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In the Supreme Court of the United States

OCTOBER TERM, 1964.

No. 20.

WALTER C. BRULOTTE and CECELIA BRULOTTE, his wife,
and
RAYMOND CHARVET and BLANCHE CHARVET, his wife,
Petitioners,

v.

THYS COMPANY,
Respondent.

BRIEF OF WELL SURVEYS, INC. (AND DRESSER INDUSTRIES, INC.) AS AMICUS CURIAE.

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I.

INTEREST OF WELL SURVEYS, INC.* AS AMICUS CURIAE.

Well Surveys, Inc. ("WSI"), on behalf of which this brief is filed, is appellee and cross-appellant in the case of *McCullough Tool Company, et al. v. Wells Surveys, Inc., et al.* (Case Nos. 6952-6956) now pending in the Tenth Circuit Court of Appeals, which was argued before that court on January 10, 1964. As indicated in our motion for leave

* The assets and liabilities of Well Surveys, Inc., including all patents owned by it and its interest in the case of *McCullough Tool Company, et al., v. Well Surveys, Inc., et al.* (Case Nos. 6952-6956, now pending in the Tenth Circuit Court of Appeals), have recently been transferred and assigned to its parent company, Dresser Industries, Inc., which is also a party to these cases. For simplicity of reference, the interest of Well Surveys, Inc. and/or Dresser Industries, Inc. as represented in this Brief as Amicus Curiae will be referred to collectively as the interest of Well Surveys, Inc.

to file this brief, such case originated as a patent infringement suit brought by WSI against McCullough, in which one of the defenses asserted by McCullough was that WSI had misused its patents by including in the royalty base of certain patent licenses granted by it operations covered by an expired patent.

The parties in the Tenth Circuit case were advised by the Court of Appeals that the decision would be "deferred pending decision by the Supreme Court of the United States in the case of *Brulotte, et al. v. Thys Company, et al.*, 376 U. S. Reports, page 905"—that is, the instant case.

In this case, this Court had, a short time previously, granted a writ of certiorari limited to two questions, of which the first is representative:

> "1. Whether it is a misuse to include in a license agreement a provision which perpetuates the monopoly of a licensed patent by a requirement that royalties be paid for the use of the invention after the patent has expired and the invention had been dedicated to the public."

The above question is so broadly stated that a categorical affirmative answer might be understood to control the decision in our Tenth Circuit case. In actuality, however, the operative facts of the two cases are very different.

In the instant *Brulotte* case, the Thys Company granted *only* package licenses with a broad royalty base including operations covered by expired patents. It apparently granted about 200 of these, in identical form, and never granted or offered any other type of license. If the characterization in the petition for certiorari is correct (we have not yet seen respondent's brief) this was a "mandatory package license."

In our Tenth Circuit case, WSI owned and offered for licensing some 60 or 70 patents relating to the logging of

oil wells by radioactivity means. Many of its licenses were granted on a standard form, which gave the licensee a right to use any of WSI's patents, or any of a designated group of them, in consideration of a specified percentage royalty based on the licensee's gross receipts from radioactivity well logging operations. Under these standard licenses, the specified percentage was applied to the licensee's total gross receipts from radioactivity well logging operations, regardless of whether individual operations had ever been patented, or whether the patents on them had expired. In view of the number of these patents which the licensees used and might use, this approach provided a convenient basis for determining the royalty due for the privilege of using all of these patents. The licensee had the right to terminate the agreement after a designated period, which was generally five years.

However, at least from June 1, 1956 on, WSI offered to all licensees and prospective licensees, by individual contact and by publication, an alternative to its standard package licenses. Each was offered the opportunity to negotiate a license under any individual patent or patents on reasonable terms, and many of such licenses were in fact negotiated. Where the licensee so desired, the royalty under a special license was made payable only on operations covered by specified patents, and the royalty on each patented operation terminated when the patent expired.

The District Court made the following finding (Finding 122, Court of Appeals Record, page 98):

> "While the royalty base employed in the standard license agreements made by WSI after June 1, 1956 included or purported to include operations covered by the expired Bender patent, the extension of the royalty base to cover practice of expired patents was not coerced, after June 1, 1956, but was voluntary upon the part of the licensees, who were offered a

real alternative by WSI's offer to grant a license under any individual patent or patents upon negotiated terms."

From a legal standpoint, the District Court concluded (oral opinion, Court of Appeals Record, page 647) that "*where there is an offer or willingness upon the part of the owner of a group of patents to license one on a reasonable royalty basis* * * * then the license agreement which has in its royalty base the payment of a royalty on service performed under expired patents is not a misuse of the patent." *

As indicated in our motion for leave, WSI's interest in the instant case arises from the fact that the question on which certiorari was granted is so broadly framed that a categorical affirmative answer might be understood to control the decision in our Tenth Circuit case, *even though it is clear in our case that the use of the broad royalty base was voluntary, and not coerced.*

II.

CONTENTION OF WELL SURVEYS, INC.

In the instant case, petitioners are contending that any inclusion in the royalty base of a patent license of operations covered by an expired patent, whether coerced or voluntary, is a misuse.

We do not know what respondent's position will be, as we have not seen its brief. It was the view of the Supreme Court of Washington that inclusion of expired patents in the royalty base, even where mandatory, is not a misuse provided the parties clearly intended such inclusion.

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* Emphasis is ours throughout this brief, unless otherwise indicated.

The present brief will be devoted to showing that, *at least where a real alternative has been offered, and a royalty base including operations covered by an expired patent is voluntarily accepted by the licensee, the patentee is not guilty of misuse.*

III.

ARGUMENT.

1. There are valid business reasons for permitting parties to a patent license to employ a broad royalty base, regardless of whether particular operations included therein are unpatented, or the patents on them have expired, and there is no sound basis for proscribing this practice, at least where an alternative is offered and the broad base is adopted by the parties voluntarily.

It is a very common practice for patent licensors, particularly where a large number of patents relating to a process, or a system, or a class of products is being licensed, to offer a license under all the patents in return for a percentage royalty on the licensee's total receipts from use of the process or system, or from sale of the line of products, without considering whether particular operations, or products, are covered by one or more unexpired patents. Licenses of this type are particularly common in industries involving a high level of research and development, such as the electronics, chemical, petroleum and radio industries, but there are few major industries which do not employ them to a substantial extent.

Such licenses—often called "field licenses"—give the licensee maximum freedom to utilize the patentee's developments in the licensed field, and at the same time provide an easily administered basis for royalty computation.

Where 50 or 100—or even 15 or 20—closely related patents are licensed, it would often be most burdensome to the parties, when trying to calculate royalties or to check royalty payments, to have to ascertain exactly which, if any, of the patents were employed in each of the licensee's operations or products. This burden is avoided by permitting the parties to agree voluntarily to a royalty rate, applicable to the licensee's gross receipts or total sales, in return for which the licensee may use any of the patents which he wishes.

It is true that gross sales or receipts in most cases include some operations or products which are unpatented, or on which the patents have expired. It is also true that this Court has often stated that convenience of the parties is no justification for an illegal act. However, we see no reason why it should be regarded as contrary to law or public policy, even in such a case, for a licensor and a licensee to agree, as a matter of mutual accounting convenience, to base royalties on the licensee's total sales or total receipts, where this basis is adopted by voluntary agreement, and the licensor is willing to base the royalty on operations covered by a particular patent, and terminate it when that patent expires, if the licensee so requests.

It should, perhaps, be emphasized that if, in such a case, operations which are unpatented, or on which the patent has expired, are included in the royalty base, the royalty calculated on total receipts is not paid *for* the right to perform an unpatented operation, or *for* the use of an expired patent. It is paid for the use of the unexpired patents or the right to use them, during the term of the license, and the broad royalty base is employed by the parties merely as a matter of accounting convenience.

2. The decision of this Court in Automatic Radio Co. v. Hazeltine is direct authority sustaining the voluntary use of a broad royalty base, regardless of the inclusion of operations which are unpatented, or on which the patents have expired.

The only case we have found in which this Court has considered the question of propriety of charging a royalty on total receipts, regardless of whether particular operations might have been unpatented, or the patent might have expired, is *Automatic Radio Co. v. Hazeltine,* 339 U. S. 827 (1950). In that case, Hazeltine offered package licenses under all its present and future patents for a flat percentage of the licensee's total sales, whether or not any of the patents were used. The license agreement included 570 patents and 200 applications. The *Hazeltine* record shows that a considerable number of these patents had expired before 1942, when the license agreement was executed; that at least half of them would expire before the end of the agreement's ten-year term (Transcript of Hazeltine Record in U. S. Supreme Court, pages 20 to 38); that some of the patents had admittedly been held invalid by federal courts before the suit on the license agreement was brought (Transcript, page 86); and that these facts were pleaded by Automatic in its answer (Transcript, page 48).

However, as stated by this Court at page 831, there was no evidence "that Hazeltine had refused to grant a license under any one or more of its patents to anyone who refused to take a license under all."

Automatic's contention was stated by this Court as follows, at page 832:

> "But petitioner urges that this case 'is identical in principle' with the 'Tie-in' cases. It is contended that the licensing provision requiring royalty payments of

a percentage of the sales of the licensee's products constitutes a misuse of patents because it ties in a payment on unpatented goods * * *."

Rejecting this contention, this Court stated at page 833:

"The licensing agreement in issue was characterized by the District Court as essentially a grant by Hazeltine to petitioner of a privilege to use any patent or future development of Hazeltine in consideration of the payment of royalties. Payment for the privilege is required regardless of use of the patents. The royalty provision of the licensing agreement was sustained by the District Court and the Court of Appeals on the theory that it was a convenient mode of operation designed by the parties to avoid the necessity of determining whether each type of petitioner's product embodies any of the numerous Hazeltine patents. 77 F. Supp. at 496. The Court of Appeals reasoned that since it would not be unlawful to agree to pay a fixed sum for the privilege to use patents, it was not unlawful to provide a variable consideration measured by a percentage of the licensee's sales for the same privilege. 176 F. 2d at 804. Numerous District Courts which have had occasion to pass on the question have reached the same result on similar grounds, and we are of like opinion.

* * * * *

"*We cannot say that payment of royalties according to an agreed percentage of the licensee's sales is unreasonable.* Sound business judgment could indicate that such payment represents the most convenient method of fixing the business value of the privileges granted by the licensing agreement. We are not unmindful that convenience cannot justify an extension of the monopoly of the patent. See, e.g., *Mercoid Corp. v. Mid-Continent Investment Co.*, 320 U. S. 661, 666; *B. B. Chemical Co. v. Ellis*, 314 U. S. 495, 498. But as we have already indicated, there is in this

royalty provision no inherent extension of the monopoly of the patent. Petitioner cannot complain because it must pay royalties whether it uses Hazeltine patents or not. What it acquired by the agreement into which it entered was the privilege to use any or all of the patents and developments as it desired to use them. If it chooses to use none of them, it has nevertheless contracted to pay for the privilege of using existing patents plus any developments resulting from respondent's continuous research. *We hold that in licensing the use of patents to one engaged in a related enterprise, it is not per se a misuse of patents to measure the consideration by a percentage of the licensee's sales.*"

3. Even if Automatic Radio Co. v. Hazeltine is regarded as involving a royalty base including only operati. which have never been patented, and not operations on which the patent had expired, the decision of this Court in Sears Roebuck & Co. v. Stiffel Company shows that there is no distinction on this ground.

Petitioners, on page 33 of their brief, try to distinguish the *Hazeltine* decision on the ground that it involved a royalty base including unpatented articles, but not articles on which the patent had expired. Petitioners go so far as to state that it is "evident from the face of the opinion that the court would have held the agreement illegal, had its attention been directed" to any inclusion of articles on which the patent had expired.

We believe the petitioners are wrong on both counts.

It is true that the majority opinion does not mention the fact that many of the sales on which royalty was required to be paid were sales of goods covered by patents which had expired, or which had been held invalid. It states the facts and contention more broadly—that many of the goods on which royalty was required to be paid

were "unpatented," and that it was Automatic's contention that this was a misuse. However, the case cannot be distinguished on this account.

As we have seen, the record in the *Hazeltine* case shows that many of the patents expired before execution of the license, that at least half of them expired during its term, that some had been held invalid, and that Automatic urged these facts in its defense. Furthermore, the dissenting justices referred, at page 840, to the public interest in "exposing invalid or expired patents," and the cases cited by the majority as authority for this Court's holding included the case of *H-P-M Development Corporation v. Watson-Stillman Co.,* 71 F. Supp. 906 (D. N. J., 1947) which expressly held that there was no legal objection to including in the royalty base articles covered by expired patents.

Finally, and by far the most important, there is no difference in principle, so far as payment of royalties is concerned, among articles covered by expired patents, articles covered by invalid patents, and articles which were never patented, *because all are equally in the public domain.*

Any possible doubt on this point was laid to rest by this Court in its unanimous decision in *Sears Roebuck & Co. v. Stiffel,* 376 U. S. 225, 84 S. Ct. 784 (1964). This Court there stated, at 84 S. Ct. 788, 789:

> "* * * when the patent expires the monopoly created by it expires, too, and the right to make the article—including the right to make it in precisely the shape it carried when patented—passes to the public.
>
> * * * * *
>
> "* * * *An unpatentable article, like an article on which the patent has expired is in the public do-*

main, and may be made and sold by whoever chooses to do so."

We submit that, in the light of both principle and the above decision, *Automatic Radio Co. v. Hazeltine* stands squarely for the proposition that a licensor and a licensee may voluntarily base royalty payments on the licensee's total receipts, even though some operations of the licensee may be unpatented, or the patent on some of them may have expired.

4. There are no decided cases holding or implying that, where the licensor offers or is willing to license on an individual patent basis, it is a misuse for the parties voluntarily to agree to base royalties on gross receipts, regardless of whether some of the included operations are unpatented or the patents have expired.

Petitioners argue on page 26 of their brief, and elsewhere, that use of a royalty base including operations covered by an expired patent is a misuse, even if such use is not coerced but voluntary. However, the many decisions cited in their brief are all cases where the patentee sought to *prohibit* the other party to a contract from practicing the invention of an expired patent, or to *compel* a licensee to include expired patents in his royalty base. None of them were cases where the patentee offered or was willing to license on an individual patent basis, but the broad royalty base was chosen voluntarily by the parties. We shall discuss the principal cases cited by petitioner.

(a) Scott Paper Co. v. Marcalus Co., 326 U. S. 249 (1945).

In the *Scott* case, this Court merely held that, when a patentee assigned his patent and was sued by his assignee for infringement, the fact that he had assigned the patent

could not estop him from defending on the ground that the device he was manufacturing was a device shown in an expired patent and therefore within the public domain.

Scott was seeking absolutely to prohibit Marcalus from practicing the disclosure of an expired patent. Had it succeeded, this would have deprived him of all opportunity to practice the disclosure, and the public of its right to benefit by his practice.

These effects do not flow from the voluntary agreement of a licensor and a licensee to base royalties on the licensee's gross receipts, without attempting to exclude operations which are unpatented or on which the patent has expired. If the potential licensee wants to perform such operations without any payment, he can do so without taking any license of any kind. If he wants to take a license under other patents of the licensor, and still perform such operations without any payment, he can request a royalty base which excludes such operations. If, as a matter of accounting convenience, he voluntarily agrees to make payment for his license under unexpired patents in the form of a royalty on his total sales, without separating out any articles uncovered by patents or on which the patent has expired, neither he nor the public is deprived of any right.

(b) Prestole Corp. v. Tinnerman Products, Inc.,
271 F. 2d 146 (6th Cir., 1959).

This case merely holds that is was misuse for patentees, in a patent pooling agreement, to forbid each other to use the licensed patents in connection with devices covered by certain expired patents. The court stated on page 155:

> "We have in mind that after the expiration of a patent, the invention originally protected thereby becomes, for all purposes, an unpatented device."

(c) American Securit Co. v. Shatterproof Glass Corp., 268 F. 2d 769 (3rd Cir., 1959):

In this case, as shown on pages 775 and 776 of the court's opinion, the patentee had consistently refused to fix a royalty on less than all of its patents, and the principal holding of the court was that this refusal to license wanted patents unless the licensee would also take a license on unwanted patents was a misuse *per se*.

However, petitioners quote on page 17 of their brief the following further paragraph of the court's opinion:

> "We conclude also, and quite apart from all of the foregoing, that paragraph 8(a) of Securit's Standard Licensing Agreement which provides that that agreement shall continue 'in full force and effect to the expiration of the last to expire of any' of Securit's patents set out in 'Schedule A' constitutes a patent misuse for it extends the payment of royalties of patents under patents which may expire to the expiration date of that patent most recently granted to Securit. Indeed the expiration clause of the contract works an 'aggravating hardship' on licensees as Judge Leahy stated, in that it demands the renunciation of all patents, whether wanted or unwanted under the license."

So far as the issue of a royalty on an expired patent is concerned, the clause in the Securit agreement is indistinguishable from the expiration clause in the Hazeltine license (Transcript, page 16). While the Hazeltine license extended for only ten years, the record showed that at least half the patents would expire before that period, so that it equally involved the payment of royalties on a broad royalty base including expired patents. There is, however, one critical fact that distinguishes the *Hazeltine* case from the *Shatterproof* case. While, in the *Shatterproof* case, no other license was available, and the licensee,

if he did not want the whole package, could get no license at all, in the *Hazeltine* case this Court regarded the package license as truly voluntary. In *Shatterproof*, the later payment of royalties on expired patents was coerced at the inception of the license. This was not the case in *Hazeltine*.

That this critical fact was in the mind of the Third Circuit Court when it wrote the paragraph above quoted, is clearly shown by the last sentence of the quotation, in which the court mentions as an additional hardship the fact that, if the licensee tried to get out of the arrangement by cancelling the license, it would mean "the renunciation of all patents, whether wanted or unwanted under the license." This manifestly refers to the licensor's unwillingness to license on any other basis than the package including expired patents.

(d) Ar-Tik Systems, Inc. v. Dairy Queen, Inc.,
302 F. 2d 496 (3rd Cir., 1962).

This is a more recent Third Circuit decision to the same effect as the *Shatterproof* decision. The patentee, as a condition of granting a license under a single patent, expressly required the licensee to continue paying royalty for a period extending beyond the expiration of the patent. There is no indication that any alternative of any kind was available to the licensee.

(e) Technograph v. Bendix Aviation Corporation,
218 F. Supp. 1 (D. Md., 1963).

In this case, Judge Watkins applied the Third Circuit's decision to invalidate an express agreement "to pay royalty under this particular patent for a period of five (5) years after its expiration." It is obvious from the opinion that the requirement was mandatory, and that there was no alternative.

(f) Scapa Dryer, Inc. v. Abney Mills,
269 F. 2d 6 (5th Cir., 1959).

This decision has little relevancy to the present case. It merely holds that, in view of the *Scott Paper* case, an ambiguous agreement should not be construed to prohibiting one of the parties from importing a patented machine into the United States after the patent expired, as such construction would render the agreement invalid.

5. **Recent District Court decisions have distinguished the above cases and have held, in accordance with the Hazeltine case, that where the licensor offers or is willing to license on an individual patent basis it is no misuse for the parties voluntarily to agree to base royalties on gross receipts, even though the patents on some of the included operations have expired.**

In every decided case in which the use by a licensor and a licensee of a royalty base of total gross receipts, without excluding operations on which the patent has expired, has been clearly voluntary, the Court has held that there was no misuse.

We have already quoted from the decision of Judge Savage in *Well Surveys, Inc. v. McCullough Tool Company,* 199 F. Supp. 374 (N. D. Okla., 1961), which distinguished the *Shatterproof* case, and relied squarely on the decision of this Court in the *Hazeltine* case.

To the same effect—and also expressly distinguishing the *Shatterproof* case—is *Eversharp, Inc. v. Fisher Pen Co.,* 204 F. Supp. 649 (N. D. Ill., Ed., 1961), in which the court concluded at page 675:

> "A license which, by its terms, continues until expiration of all of the patents covered by such license, does not constitute a patent misuse, in the absence of

a showing of coercion on the part of the patent owner that the licensee accede to such a provision."

Another case so holding is *Carter Products v. Colgate-Palmolive Co.*, 164 F. Supp. 503 (D. Md., 1958). There, just as in the *Shatterproof* case, the royalty was to continue undiminished until the expiration of the latest of the licensed patents. However, the court distinguished the *Shatterproof* decision and held that there was no misuse stating at page 525:

> "In the case at bar, there is no evidence that plaintiffs would issue a license under the basic Spitzer patent *only** on condition of an acceptance by the licensee of a provision including any other patent."

Petitioners argue on page 31 of their brief, that the above District Court decisions are erroneous because the courts have "failed to perceive the distinction" between block booking "in which coercion by the patent owner may be a necessary element of misuse" and inclusion in the royalty base of operations covered by expired patents, which petitioners contend is a misuse even where wholly voluntary.

It is our position that the alleged distinction is a distinction without a difference. None of the decisions cited by petitioners requires a holding that, in a case where the patent owner offers, or is willing, to license on an individual patent basis, it is a misuse for the parties, for the sake of accounting convenience, to agree voluntarily to base royalties on total gross receipts, without excluding operations which are unpatented, or on which the patents have expired. Any such holding would be contrary not only to the above District Court decisions, but also to the express holding of this Court in the *Hazeltine* case. As we have indicated, where such a royalty base is used volun-

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* Emphasis is the court's.

tarily, the royalty calculated on total receipts is not paid *for* the right to perform an unpatented operation, or *for* the use of an expired patent—it is paid for the right to use the unexpired patents during the term of the license, and the broad royalty base is employed merely as a convenient way for measuring the value of the patents actually licensed.

It is only when package licensing, or the use of the broad royalty base, is made mandatory by the patent owner, that the licensee or the public is deprived of any rights, or that there is a patent misuse.

IV.

CONCLUSION.

We express no opinion as to the validity of the view taken in this case by the Supreme Court of Washington. However, if this Court concludes that the use by the parties of the broad royalty base in the instant case was truly voluntary, we believe, in the light of what we have stated in this brief, that the decision should be affirmed. And, even if this Court should decide to reverse it, we believe it should do so in terms which do not foreclose a case in which it is clear that the patent owner offered or was willing to license on an individual patent basis, but the broad royalty base was voluntarily chosen by the parties for accounting convenience.

Respectfully submitted,

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